# Investment asset amounts, allocation and returns by the end of the first quarter of 2013

**Investment portfolio in state of continued growth due to favourable market conditions**

The combined investment portfolio of earnings-related pension investments amounted to EUR 154.8 billion at the end of March 2013. Primarily by way of good profits, the investment portfolio experienced steady growth in all earnings-related pension community groups. The accrued growth in total was EUR 5.2 billion. Such a favourable development during the first quarter provides a solid foundation for the rest of the year. Over the years (2004-2012), the average annual rate of growth of the investment portfolio has been EUR 7.7 billion.

The growth in the investment portfolio was affected by good development in the financial markets over the early part of the year. Support measures offered by central banks have continued to aid the international financial markets, especially the stock markets. Promissory notes with credit risk have also managed well; better than state loans with good credit ratings that have, to some degree, suffered from the rise in the interest rate level. The support of the central banks will be needed also going forward, since the economic atmosphere remains uncertain. Economic growth, especially in the Euro zone, has yet to pick up speed. Management of the European debt crisis also requires continued measures.

**Allocation changes in the sector point to improved risk tolerance**

**More shares, less investments in interest-bearing instruments, stable real estate**

The allocation structure of the entire investment portfolio was as follows at the close of March 2013 (the situation at the end of 2012 in brackets): investments in interest-bearing instruments 44.9% (46.5%), share investments and similar 44.5% (42.7%) and real estate investments 10.6% (10.8%).

**From money market investments to shares**

The allocation of shares and share-like investments in the sector grew by 1.8 percentage points, a total of EUR 5.1 billion. Money market investments decreased by EUR 2.0 billion. This change is typical in a market environment on the upsurge, where share investments have increased in value. Good development in the financial markets and general expectations for this trend to continue have served to improve risk tolerance. Funds have been transferred from low-risk (domestic) money market investments, easily transformed to cash, to share investments (outside the Euro zone). The drop in money market investments largely came from the portfolios of the companies, but also from actors in the public sector. The growth of listed shares was formed from the portfolios of all earnings-related pension community groups.

**Changes inside share allocation: more listed shares (incl. funds) and hedge funds, fewer share investments of other types**

The growth in hedge funds, stronger than before, is also a sign of improved risk tolerance. Although the share of listed shares (incl. funds) and hedge funds has grown, the share of other share investments has simultaneously shrunk due to the decreasing net value of derivatives. The growth in popularity of hedge funds and subsequent decrease in other share investments stemmed primarily from the portfolios of companies, but also from those of public-sector actors.

**Investment and TyEL premium lending portfolios diminished, low number of new loans**

The different forms of financing - investment and TyEL premium lending – offered by pension insurance companies continued to diminish in early 2013. The total EUR amount of new loans was lower than normal. The situation shows that the availability of financing for companies has remained at a good level.

**From domestic targets to targets outside the Euro zone**

The medium-term trend, a gradual transfer towards countries outside the Euro zone, continued during the first quarter of 2013. The background for this shift in regional focus is the impact of the Euro zone crisis and an extremely low interest rate environment, leading to the active transfer of investments to targets where the risk/reward ratio is more optimized. New investment targets have been found in e.g. developing markets, where faster economic growth creates better profit-making opportunities for investors. During the first quarter of 2013, the sector as a whole experienced a shift of 2.3 percentage points when the weight of targets outside the Euro zone increased to 44.6 per cent and the weight of Finland decreased to 29.6 per cent. The weight of the Euro zone (excl. Finland) remained as it had been at the close of 2012: at 25.9 per cent.

**Finland allocation in downward tilt – companies decreasing their money market and share investments**

When examining the development of the share of Finland investments from the end of 2000 to the end of the first quarter of 2013, it becomes clear that the current situation is tilting downwards in the fluctuation range (28.6% - 59.1%). The Finland allocation of the sector decreased by a total of EUR 1.9 billion during the first quarter. This decrease, and other changes of the first quarter,are almost exclusively the result of actions taken by earnings-related pension insurance companies in the private sector.

The most significant impact of the shrinking allocation of domestic investments came from money market investments that were diminished by a total of EUR 1.8 billion in the sector as a whole. Aside from money market investments, the number of other investments in interest-bearing instruments also dropped, by a total of EUR 0.6 billion, as investment and TyEL premium lending decreased and the bonds of the Finnish State were sold. However, the largest sale concerned shares, that were viewed quite differently among the earnings-related pension communities: the private sector sold, whereas in the public sector, selling and buying went end to end.

**New investments outside the Euro zone: listed shares a favourite investment in the private sector, bonds in the public sector**

The amount of investments outside the Euro zone in this sector grew by EUR 5.8 billion during the first quarter of 2013. Additional acquisitions explain 70 per cent of this increase, and the rest stems from improved market valuations. The public sector emphasized investments in interest-bearing instruments, bonds from financial institutions and mutual funds in their purchases, whereas the private sector focused on shares listed by companies (including funds).

## Companies bought state bonds in Euro zone (excl. Finland)

The weight of sector investments in the Euro zone (excluding Finland) remained at the level of the end of 2012, in other words 25.9 per cent. In euros, the amount of these investments grew by EUR 1.4 billion. The growth came almost solely from earnings-related pension company expansions. Other earnings-related pension insurer groups sold. Both the companies purchasing and the public sector selling focused on bonds over shares. New acquisitions of investments in interest-bearing instruments focused on the bonds of public sector entities (excl. Finland), in other words, state bonds and bonds of issuers tied to the state. Several guesses can be made regarding this crisscrossing behavior. One explanation might be that actors now have different opinions on future development, regarding e.g. the crisis in the Euro zone, the low interest level and the economic development. These differences in viewpoint translate into different portfolios and changes to portfolios.

## The start of a year of good returns

The eight largest earnings-related pension providers succeeded well in their investments during the first quarter of the year. The total return fluctuated between 1.2% and 3.8%. The average total return of the two largest public-sector pension providers was 3.6% and the corresponding figure for the six largest earnings-related pension companies was 2.6%. There are solvency regulations in place for earnings-related pension insurers in the private sector, whereas their counterparts in the public sector are not subject to solvency regulations.

The best average rate of return per group came from share investments: 7.3% for the public sector and 5.9% for companies. The public sector has succeeded especially well with listed shares (7.8%) and the companies with both unlisted (8.0%) and listed shares (6.4%). Also for these good returns, an explanation can be found in the global, positive development trend of the stock markets that dominated the early part of the year. Good rates of return have been achieved also in hedge fund investments (companies 3.6% and public sector 3.2%). The more modest rates of return seen in investments in interest-bearing instruments, on the other hand, have been affected by the extremely low interest level.

Good returns can be seen also in the long term. The average annual real return of the entire sector is 4 per cent, calculated over the period from the beginning of 1997 to the end of the first quarter of 2013. For earnings-related pension companies, the corresponding rate of return is 3.8, for public-sector pension insurers it is 4.3. The Finnish Centre for Pensions uses 3.5 per cent as the assumption of real return in its long-term projection.

## Solvency on a firm foundation

During the first quarter, solvency was at a strong level, and increasing in strength for almost all actors. Solvencies have been calculated using new solvency legislation that came into force in the beginning of 2013. A temporary Act that was implemented as a result of the financial crisis remained valid until the end of 2012.

## Outlook for the remainder of 2013

Pension insurers are fairly unanimous in their view of the expected development of investment returns where the end of the year is concerned. Development is expected to be more moderate than during the first quarter. Familiar worries are lurking in the background: insecurity regarding global financial growth, and continued debt problems in the Euro zone.